

Economic Analysis of Standards for ROW Fees

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Public Scoping Meeting

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Study on Indian Land and Rights of Way

Cameron Bio

- Ph.D. economist with extensive experience in gas, oil and electricity policy issues
- Economic consultant for past 10 years
- Asst. Professor at Carnegie Mellon University
- Numerous articles on energy industry economics published in leading academic and professional journals

Executive Summary

- Key policy question: How do we reduce overall cost of meeting national energy needs?
 - ◆ Greater efficiency enlarges economic pie available for all
- Important step: introduce more transparent, cost-based standards for ROW fees on tribal trust lands
 - ◆ Firm investment incentives improved
 - ◆ Significant source of risk removed, increasing project viability
 - ◆ Upward pressure on rates reduced

Outline

- Economics of transportation infrastructure
- Current standards for ROW fees
 - ◆ US private lands
 - ◆ Federal, state and municipal lands
- Impact of gap in standards for determining ROW fees on tribal trust lands

Energy Transporters Serve Vital Economic Function

- Natural gas/oil pipelines transport commodity from producing areas to end-users
- Electric transmission lines carry power from generators to load
- Capital intensive facilities
 - ◆ Regulated at federal and/or state level
 - ◆ Regulated rates based on cost of service to protect consumers
 - ◆ Cost recovery allowed for transportation providers to attract efficient investment

Standards for ROW Fees on Private Lands Support Infrastructure Investment

- Energy transporters have long had right of eminent domain on private lands to obtain required easements for projects deemed to be in public interest
- Landowner is compensated for loss in market value of land impacted by easement
- Easements typically provided in perpetuity

Similar Standards for ROW Fees Apply Outside Private Lands in US

- Areas within US in which energy transporters do not have eminent domain include
 - ◆ State lands
 - ◆ Federal lands administered by Bureau of Land Mgmt, US Forest Service, or National Park Service
 - ◆ Municipal lands
- In these areas, standard is that ROW fees approximate lost value of property, even without eminent domain

Transparent, Efficient Standards for ROW Fees Create Public Benefits

- Landowners made whole
 - ◆ Compensation based on lost market value of property
 - ◆ Compensation covers property damage
- Compensatory ROW fees do not reflect monopoly prices for land
 - ◆ Energy transporters have economically desirable incentives for meeting demand
 - ◆ Energy infrastructure can follow least cost routes

Lack of Standards Raises Costs of Meeting National Energy Needs

- Tribal trust lands lack transparent, efficient standards for determining ROW fees
- As a result, some tribes may be overpaid or underpaid relative to the compensatory amount
- **Both** underpayment and overpayment increase cost of meeting our national energy needs
- Focus on overpayment case

How Does Lack of Standards Raise Costs? "Hold Out"

- Some tribal lands strategically located between energy producers and end users (generators and load)
 - ◆ Incentives to capture much of public benefit associated with project
 - ◆ Tribes can "hold out" for just below build around costs
- Current policy defeats purpose of compensatory ROW fees enforced on rest of project route

How Does Lack of Standards Raise Costs? Renewals

- For incumbent infrastructure providers
 - ◆ Companies willing to operate as long as $\text{price} \geq \text{average variable cost}$
 - ◆ Tribes can charge renewal fees that leave companies with no more than this margin
 - ◆ Companies trapped. Might never have built on tribal trust lands if they had foreseen current regime
- For new entrants
 - ◆ Enormous uncertainty on horizon
 - ◆ Otherwise beneficial projects can become financially nonviable

Lack of Standards: Negative Economic Impacts

- Companies can abandon proposed lines when
 - ◆ Tribal demands render lines unprofitable or too risky to be viable
 - ◆ "Build around" is too expensive
- Companies have incentive to choose more costly routes to bypass tribal trust lands
- Companies/tribes devote significant resources to lengthy negotiations and renegotiations
- Result: too little transportation infrastructure is built at too high a cost

Renewals: Negative Economic Impacts

- Many transporters can pass increased tribal ROW fees on to consumers
 - ◆ Tribes can use rate-making methodology to harm consumers
- If increased ROW fees cannot be passed through
 - ◆ Transporters face reduced returns, lose ability to attract capital
 - ◆ Underinvestment raises long run costs to all energy consumers

Tribes Benefit from More Transparent, Efficient Standards for ROW Fees

- High costs/uncertainty/delays associated with current regime signals to infrastructure investors:
 - ◆ Don't build here
 - ◆ Don't invest here
 - ◆ Don't create jobs here
- More efficient, more transparent standards
 - ◆ Contribute to improved climate for development on tribal trust lands
 - ◆ Ensure that no tribe receives less than compensatory value for ROW

Recap

- Energy transportation infrastructure is vital to economy
- Transparent, cost-based standards for ROW fees on tribal trust lands will
 - ◆ Reduce overall cost of meeting national energy needs
 - ◆ Improve investment incentives
 - ◆ Remove significant source of investor uncertainty, increase project viability
 - ◆ Mitigate upward pressure on rates